2022 Global Meeting of the Emerging Markets Forum

Navigating in a Fast Moving and Turbulent World

16-18 May 2022, Banque de France-Marriott Opera Ambassador, Paris

Keynote Speech by Ngozi Okonjo-Iweala,
Director General, World Trade Organization (WTO)

NAVIGATING THE POLYCRISIS: TRADE IS PART OF THE SOLUTION

Dr Ngozi Okonjo-Iweala at the Banque de France/ Emerging Market Forum

16 May 2022

- Excellencies, it has become a cliché to say we live in an interdependent world – but it is no less true for that.

- The complex web of trade, financial and other ties linking countries and regions means that, whether we are central bank governors, finance ministers, or trade officials, our decision-making processes have to take into account factors outside our respective policy fields.

- When the GATT morphed into the WTO and its founding agreements were being negotiated some 27 years ago, trade ministers explicitly recognized that growing interactions between the structural, macroeconomic, trade, financial, and development aspects of economic policymaking meant that, and I quote, "successful cooperation in each area of economic policy contributes to progress in other areas".

- The words of this so-called 'coherence mandate' for the newly transformed WTO, the IMF, and the World Bank resonate amid our current "poly-crisis." Simultaneous crises in public health, global security and the environment have major ramifications for economic growth, trade, financial and price stability, poverty and hunger. Compounding crises demand multifaceted but coherent responses, from public institutions as well as the private sector.

- Policymakers and leaders must reflect on these linkages. Fora like this one help foster the dialogue we need.

- This evening, I will make three points:

    - First, trade is central to economic growth and recovery from the present crises.

    - Second, while it has become increasingly fashionable to point the finger at trade for different problems we face, the reality is that trade is part of the solution to the global commons challenges that threaten people's future living standards.

- Third, to foster the international economic cooperation we need, the world needs to invest in the Multilateral Trading System and the WTO, and ensure complementarity between macroeconomic and trade policies.

I will also share some reflections about the implications of tightening monetary conditions for trade policy.

1. **Starting with my first point, trade features prominently in the current crises – and in recovery from them.**

   Trade was critical to the growth rebound we saw in 2021. Merchandise trade volume growth of 9.8% (contributed to the 6.1% rate of global GDP growth. For developing and emerging markets in particular, external demand was a key driver of growth.

- The Omicron variant and the war in Ukraine have darkened the global economic outlook for 2022. International organizations have all downgraded their forecasts. In April, the IMF cut its forecast for world GDP growth by 1.3 percentage points from what it was last October, to 3.6%.

- At the WTO we have also revised our trade forecasts downwards. Global merchandise trade volumes are projected to expand by only 3% this year – last October we had predicted 4.7%. We are projecting a 3.4% expansion for 2023 but all this is subject to a great deal of uncertainty due to the war in Ukraine and the still-ongoing pandemic, with most risks on the downside.

- This is supported by GDP data from China, Europe and the United States, as well as real-time trade indicators like port throughput indices, all point to a slowdown of output and trade in the first quarter of 2022.

- The slower pace of economic recovery in many low- and lower-middle-income countries that became apparent last year – a legacy of differing fiscal capacity and vaccine access across regions - remains visible in the trade data.
  - According to our forecasts, in Africa, the volume of merchandise imports in 2022 is set to be 5.8% lower than in

2019, before the pandemic. The continent's export volumes are projected to fall by 1.4% over the same period.
  - By comparison, Asia's merchandise imports will have increased 12.2% and its exports will have risen 16.7% over the same period.
  - North America's imports and exports are expected to increase by 9.9% and 0.3%, respectively. Meanwhile, Europe's imports will grow by 3.9% while its imports expand 2.4%.

- These divergences may be poised to get worse.

  Prices for food, fertilizers and energy, for which Ukraine and Russia are important suppliers, were already on the rise last year. With the war, they have risen to dangerously high levels, adding to the economic pain from tightening monetary conditions. Food importing low-income countries face serious risks of hunger, particularly those countries highly dependent on food imports from Russia and Ukraine. For example, more than half of wheat imports in Egypt, Lebanon and Tunisia come from Russia and/or Ukraine. 35 countries in Africa import food and 22 import fertilizer from the Black Sea region.

- The COVID-19 lockdowns in China, and the potential for new variants worldwide, remind us that only 13% of people in low-income countries are fully vaccinated against COVID-19, and 51% of people in lower-middle-income countries, compared to 73% of people in high-income and upper-middle-income countries. While vaccine production has increased, serious problems persist in terms of countries' absorption capacity, as well as individual hesitancy.

- Pandemic-related supply chain disruptions are now being aggravated by the war in Ukraine, adding to concerns about supply chain fragility. The 500 ships that were waiting outside the world's largest port of Shanghai last week are a case in point. Citing data from Project 44, a shipment tracker, the Financial Times reported this week that average waiting time for import containers in Shanghai was 12.9 days on May 12, a 174 per cent increase from the end of March.

- World shipping rates remain elevated amid port closures and stubborn labour shortages. Although costs have come down a bit since earlier this year, today it would cost over $9800 to ship a forty-foot container from Shanghai to Rotterdam - about ten times more than it would have cost in 2019. After easing somewhat, delivery times are also rising again. Given that the WTO estimates that transport and travel costs account for 20 to 30 per cent of total trade costs across sectors, sustained upward pressure on transport costs will both add to overall cost pressures and weigh on the trade recovery. The IMF estimates that higher shipping costs have added 1.5 percentage points to inflation projections for this year.

2. **This brings me to my second point, namely that trade is an important part of the solution to tackling current challenges.**

- This may come as a surprise to the growing chorus of voices blaming trade for supply shortages and inflation, as well as a litany of other woes.

- Let's look more closely at some of these claims. The reality is that for decades before the pandemic, global value chains were disinflationary: more foreign competition squeezed domestic firms' mark-ups, and greater participation by low-cost producers meant lower imported inflation.

  It is true that during the pandemic, supply chain bottlenecks became a source of inflationary pressures. But much of this was due to a mismatch between demand and supply, as the massive fiscal impulse and sudden changes to consumption patterns pushed aggregate demand, particularly for durable goods, beyond the capacity of producers to respond. Supply-side factors like lockdowns and labour shortages also played a role.

- At the same time, almost since the beginning of the pandemic, trade has been a lifeline for producing and accessing critical medical supplies from face masks to vaccines. COVID-19 vaccines in particular are made in multi-country supply chains – 19 countries each for the Moderna and Pfizer/BioNTech vaccines.

Less trade would have almost certainly meant fewer vaccine doses, and consequently less resilience and health security.

- Food trade had held mostly stable through the pandemic - until the war in Ukraine. International cooperation on trade will be key to prevent current market tensions from turning into full-fledged food shortages.

  Trade is necessary to move supplies of grain and oil from where they are abundant to places where they have been withdrawn from the market as a result of the war. The WTO is closely monitoring developments in food trade and is part of the UN Secretary-General's Steering Committee of the Global Crisis Response Group on Food, Energy and Finance.
  We have been urging members to refrain from placing export restrictions on food, which have in the past made price spikes worse. We are also encouraging countries with ample buffer stocks to release some onto international markets. That said, our monitoring suggests that 22 countries have introduced 41 food-related export restrictions since the war started in late February, including 10 measures introduced since the 29th of April.

  It's worth mentioning that drought in different parts of the world is a significant factor in rising food costs. Trade is an important means for adapting to climate change as well as cutting emissions – importing supplies after a natural disaster, spreading cutting-edge technologies around the world, or fostering the competition that helps bring down prices. The multi-trillion-dollar, multi-decade global push we need for a successful low-carbon transition could give rise to what some have dubbed "greenflation" in key raw materials and inputs. Cooperation on trade could help identify and address supply bottlenecks and ensure green investment remains as cost-effective as possible.

3. **My third point is that a broad retreat from trade would not be likely to achieve its stated goals. A better option is to invest in the multilateral trading system and back it up with coherent macroeconomic policies. The multilateral trading system is in my view a global public good created 75 years ago and nurtured over decades. We must not take it for granted.**

- We increasingly hear claims that the way to respond to the current crises is by re-shoring, near-shoring, or friend-shoring supply chains. The new catchphrase is "secure trade."

- There will undoubtedly be some re-shoring and friendshoring, given the world of simultaneous crises we live in. And some near-shoring had already been underway as China's labour costs increased substantially, and as businesses altered risk vs. efficiency strategies to ensure certainty of supply – a bit less just-in-time, and a bit more just-in-case.

- But there is little evidence thus far in WTO data of reshoring. If we take the US-China trade as an example, merchandise trade between the two has been at historic highs. US merchandise exports to China broke records last year at $153 billion, while US imports from China at $542 billion were not far from the 2018 peak of $563 billion.

- We know there are moves to reshore the semiconductor industry through massive subsidies, and something similar may happen for some medical supply chains. But make no mistake: taking reshoring and friend-shoring too far would almost certainly fail to achieve the stated objectives of managing supply chain risks.
  - Purely domestic supply chains would be more vulnerable to localized shocks like climate disasters or disease outbreaks.
  - We cannot be sure that less trade would foster more geopolitical harmony – indeed, modern Europe's experience has been predominantly the opposite, despite the current experience with Russia and gas, which less a warning about trade as such than about the dangers of overconcentration.

- Moreover, far-reaching de-globalisation would have major economic costs. WTO economists have done some simulations for what would happen if the world economy were to breaks into two trading blocs.
  - The diminished specialization and technology spillovers alone would lower the long run level of real global GDP by about 5%. For the sake of comparison, the global financial crisis of 2008-09 lowered OECD countries' long-run potential output by an estimated 3.5%.
  - And the losses would not end there. Additional losses would come from reduced scale economies, transition costs for

businesses and workers, disorderly resource allocation, and financial distress – not to mention the prospect of new trade barriers within each bloc.

- Worst of all, decoupling would be particularly damaging for lower-income countries, which have the most to gain from technological spillovers associated with trade. The pandemic has already reversed 25 years of income convergence between poor and rich countries. Trade decoupling would entrench this renewed divergence.

- A more promising path towards supply resilience and security would be through deeper and more diversified international markets – suppliers in more places, carrying more inventory, and more flexible production capacity. Re-globalization, not de-globalization.

- For this, we need well-functioning supply chains – which is why the WTO is working with shipping companies, port operators, logistics firms, and other businesses to find solutions to the current disruptions.

- We also need a strengthened, open, multilateral trading system – one in which more countries and communities are brought from the margins to the mainstream of the global division of labour.

- In the past decade, we have seen low-to-middle income countries in central Asia, Latin America, the Mekong region, and Africa become new and reliable suppliers to supply chains, offering development opportunities to local populations.

- We need to extend this further, to encompass other countries, regions, and groups like women and small businesses. Such 're-globalization' would help drive diversification and resilience globally, while contributing to growth and poverty reduction in the countries that need them most.

Conclusion: act together to foster resilience

- Re-globalization will take time, however, and in the short run, the international community must work together to respond to challenges that cut across the lines of our respective economic policy fields.

  - For example, in the face of the external shock to international food prices, we must ensure that the poorest countries receive adequate financial support to avoid balance of payment crises or bankruptcy. People's living conditions are already deteriorating as a result of inflation.
  - Access to trade finance by many low-income countries has become more difficult since the beginning of the pandemic. Multilateral development banks (MDBs) have had to step in to ensure that essential food and medical supplies could reach the poorest countries.
  - And while financial sanctions have excluded trade in food products, practical difficulties in processing supplier payments, resulting from cautious behaviour by financial operators, have reportedly affected commercial clients as well as the World Food Program.

With central banks from the US and UK to India and Brazil having already raised rates, and even the ECB set to follow suit, I want to think out loud a bit about the implications for trade and trade policy.

We are, of course, all mindful of the difficult trade-off that central banks confront in developed and developing countries: between supporting a still-fragile recovery now battered by new shocks from Ukraine, and reining in inflation before it develops into wage-price spirals.

- The experience from the monetary tightening in the late 1970s and early 1980s reminds us that for low- and middle-income economies, the risk of capital flight and balance of payments crises is real.
- Back then, many developing countries' first instinct in the face of balance-of-payments problems was to tighten import restrictions. These policies were not effective - they increased hardship for local populations, while failing to address the fundamental causes of external imbalances.
- But as the Dartmouth economist Doug Irwin describes in a recent NBER working paper, by the early 1980s, foreign exchange had become so scarce – from borrowing, aid, and trade - that further import repression was no longer a viable option. In many places, this spurred governments to reorient policy from trying to conserve foreign exchange to trying to earn more of it. Instead of

trying to limiting imports to manage the balance of payments, countries let the exchange rate adjust instead.

- This was nothing less than an intellectual revolution. I would not be surprised if Montek can still remember something Indian Prime Minister PV Narasimha Rao said about the country's big reform package in 1991: "you cannot import if you do not export… My objective is to make India truly self-reliant. Self-reliance is not a mere slogan for me. It means the ability to pay for our imports through our exports."
- The wave of market reforms within developing countries from the mid-1980s through the mid-1990s coincided with the Uruguay Round GATT negotiations, and ultimately helped many of these countries take advantage of the transparent and predictable trading environment provided by the WTO. The ensuing growth helped lift over a billion people out of poverty.

- But many poor countries were left out of these gains, as were many poor people in rich countries. Today these poor countries are susceptible to commodity price volatility and capital flight. They would benefit from more integration into regional and global supply chains, and especially from more diversification and value addition, which would make for more stable export earnings. This requires a strong multilateral trading system. Ongoing regional processes, such as the African Continental Free Trade Area, could also help foster greater trade integration.

- My broad point is that trade and macroeconomic variables are intimately linked. Trade helps allocate resources more efficiently within and between countries, and helps improve productivity, efficiency and economic integration between countries – with positive effects on the "convergence" of standards of living. Meanwhile, countries that experience greater volatility in inflation and exchange rates tend to be less integrated.

- Let me close by noting that these linkages are embedded in our founding agreements. I started by mentioning the WTO coherence declaration from 1994, but I could just as well have mentioned Article 1 of the IMF, adopted at Bretton Woods exactly 50 years earlier. It calls for promoting international monetary cooperation [..] to facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income

> and to the development of the productive resources of all members as primary objectives of economic policy."

At this fraught geopolitical moment, let us all remember the lessons of history. Let us remember why our multilateral economic system was created almost eight decades ago. It is time to invest in modernizing and upgrading that system – not to retreat from it. The multilateral trading system, the multilateral institutions are, I repeat, global public goods. We must not take them for granted.

- Thank you.